113 FERC ¶ 61,265
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeen G. Kelly.

Nevada Power Company
GenWest LLC

Docket No. EC05-132-000

ORDER AUTHORIZING DISPOSITION AND ACQUISITION OF FACILITIES

(Issued December 15, 2005)

1. On August 31, 2005, Nevada Power Company (Nevada Power) and GenWest, LLC (GenWest) (collectively, Applicants) filed an application under section 203 of the Federal Power Act (FPA)[1] for authorization for disposition and acquisition of jurisdictional facilities in connection with the sale of a 75 percent interest in the Silverhawk Power Station (Silverhawk Station) from GenWest to Nevada Power. The jurisdictional facilities consist of interconnection facilities and generator step-up transformers. The Commission has reviewed the proposed transaction under the Commission's Merger Policy Statement.[2] We will authorize the proposed transaction, as we find that it will not have an adverse effect on competition, rates or regulation and is thus consistent with the public interest.

[1] 16 U.S.C. § 824b (2000). The Energy Policy Act of 2005 (EPAct 2005) repeals the Public Utility Holding Company Act of 1935 (PUHCA 1935), and enacts the Public Utility Holding Company Act of 2005 (PUHCA 2005). EPAct 2005, §§ 261 *et seq.*, Pub. L. No. 109-58, 119 Stat. 594 (2005). We have analyzed this transaction under section 203 as it appears pre-EPAct 2005, since the amended section 203 does not become effective until February 8, 2006.

[2] *Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement*, Order No. 592, 61 Fed. Reg. 68,595 (1996), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,044 (1996), *reconsideration denied*, Order No. 592-A, 62 Fed. Reg. 33,341 (1997), 79 FERC ¶ 61,321 (1997) (Merger Policy Statement); *see also Revised Filing Requirements Under Part 33 of the Commission's Regulations,* Order No. 642, 65 Fed. Reg. 70,984 (2000), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,111 (2000), *order on reh'g*, Order No. 642-A, 66 Fed. Reg. 16,121 (2001), 94 FERC ¶ 61,289 (2001) (Merger Filings Requirements Rule).

I. Background

A. Description of the Parties

2. Nevada Power is a public utility and a wholly-owned subsidiary of Sierra Pacific Resources, an investor-owned public utility holding company. Nevada Power engages in the generation, transmission and distribution of electricity, serving more than 738,000 electricity customers in southern Nevada. According to Applicants, Nevada Power is the nation's fastest growing electric utility in terms of annual percentage growth. Applicants note, however, that Nevada Power is able to serve only 24 percent of its peak load from its own resources because it owns only 2,051 megawatts (MWs) of generating capacity. Applicants state that the remaining 63 percent of Nevada Power's peak load is supplied from existing contracts or power purchased in the regional wholesale market. According to Applicants, this exposes Nevada Power and its customers to risk vis-à-vis price and reliability.

3. GenWest is a limited liability company and a direct, wholly-owned subsidiary of Pinnacle West Energy Corporation (PWEC), which, in turn, is a direct, wholly-owned subsidiary of Pinnacle West Capital Corporation (Pinnacle West). GenWest is a special purpose subsidiary formed to construct and own the Silverhawk Station, and is authorized, under section 205 of the FPA,[3] to sell capacity, energy, and ancillary services at market-based rates.[4] The Silverhawk Station is a 560-MW natural gas combined cycle power plant located in Nevada Power's control area. GenWest owns a 75 percent undivided interest in the Silverhawk Station; the remaining 25 percent undivided interest is owned by Southern Nevada Water Authority (Water Authority), a municipal subdivision of the State of Nevada.

B. The Proposed Transaction

4. Applicants have a purchase agreement under which GenWest will sell to Nevada Power GenWest's 75 percent ownership interest in the Silverhawk Station and associated jurisdictional assets such as interconnection facilities and generator step-up transformers necessary for power to be delivered from the Silverhawk Station to the Nevada Power transmission grid. Upon completion of the proposed transaction, Nevada Power will hold a 75 percent interest in the Silverhawk Station, and the Water Authority will continue to hold its 25 percent interest in the facility. Nevada Power will assume operating

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[3] 16 U.S.C. § 824(d) (2000).

[4] *See GenWest LLC*, Docket No. ER03-352-000, unpublished letter order (June 6, 2003).

responsibility from PWEC under a facility operating and maintenance agreement.[5] According to Applicants, the proposed transaction will reduce Nevada Power's reliance on purchased power by increasing generation owned by Nevada Power, thereby reducing costs and enhancing reliability for its customers

II. Notice of Filing and Responsive Pleadings

5. Notice of Applicants' filing was published in the *Federal Register*, 70 Fed. Reg. 53,788 (2005), with comments, protests or interventions due on or before October 14, 2005. The Water Authority and Nevada Bureau of Consumer Protection filed timely motions to intervene on October 14, 2005. Neither entity protests the proposed transaction.

III. Discussion

A. Procedural Matters

6. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

B. Consistency with the Public Interest

7. Section 203(a) provides that the Commission must approve a disposition of facilities if it finds that the disposition "will be consistent with the public interest."[6] The Commission's analysis under the Merger Policy Statement of whether a consolidation is consistent with the public interest generally involves consideration of three factors:

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[5] Applicants note that Nevada Power also will assume an existing Interconnection and Operation Agreement between GenWest and Nevada Power under Sierra Pacific Resource's Open Access Transmission Tariff (OATT), as well as the existing Service Agreement for Long-Term Firm Point-to-Point Transmission Service between Nevada Power and Pinnacle West. In addition, Applicants state that Nevada Power will assume an agreement between Reliant Energy Services, Inc. (Reliant) and GenWest under which Reliant has the option to transfer a Service Agreement for Long-Term Firm Point-to-Point Transmission Service to GenWest in 2009 and GenWest has the option to retransfer the agreement back to Reliant in 2014.

[6] 16 U.S.C. § 824(b) (2000) [new citation pending].

(1) the effect on competition; (2) the effect on rates; and (3) the effect on regulation.[7] As discussed below, we will approve the proposed transaction as consistent with the public interest because it will not adversely affect competition, rates, or regulation.

1. Effect on Competition

a. Applicants' Analysis of Horizontal Competitive Issues

8. Nevada Power retained Dr. Peter Fox-Penner[8] to analyze the effect of the merger on competition. Dr. Fox-Penner states that the relevant products are primarily short-term, non-firm energy products. He concludes that the proposed transaction does not raise any competitive concerns when changes in market concentration are computed for energy product definitions which take account of Nevada Power's native load obligations (*i.e.*, Available Economic Capacity).

9. Dr. Fox-Penner identifies the Nevada Power control area and all first-tier control areas (Arizona Public Service Company, Los Angeles Department of Water and Power, PacifiCorp-East, California Independent System Operator's Path 15, Western Area Power Administration-Lower Colorado) as relevant geographic markets using the approach described in Appendix A of the Merger Policy Statement.[9] He uses the Delivered Price Test to evaluate the effect on competition in the relevant markets for 14 distinct time periods, from summer superpeak hours to off peak hours in the four traditional seasons. For the Nevada Power control area, he uses a range of prices from $37.18 per megawatt hour (MWh) in the Fall Off-Peak period to $99.75 per MWh in the Summer_50 period.[10] He estimates 2006 fuel costs as the product of the unit's heat rate and projected fuel prices for 2006, the test year for the analysis. He estimates 2006 coal prices based upon plant-specific fuel prices taken from 2003-2004 Monthly FERC Form 423. He estimates nuclear and other fuel prices using either FERC Form 1 or FERC Form 423 data and escalating to 2006 using historical rate price changes between 2003 and 2004.

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[7] *Supra* note 1.

[8] Dr. Fox-Penner, an economist, is a Principal and Chairman of The Brattle Group, an economic and management consulting firm. Dr. Fox-Penner was retained by Nevada Power to analyze the competitive effects of its acquisition of GenWest's 75 percent share of the Silverhawk Station.

[9] 18 C.F.R. § 33.3(c)(2) (2005).

[10] He defines the Summer_50 period as the highest 50 hours of hourly spot prices likely to be observed in a destination market in Summer. *See* Fox-Penner Affidavit at P 30.

10. Dr. Fox-Penner states that there are no failures of the Competitive Analysis Screen[11] for either Economic Capacity or Available Economic Capacity in Nevada Power's first-tier control areas.

11. Turning to the Nevada Power control area, Dr. Fox-Penner finds screen failures for Economic Capacity in 11 of the 14 time periods studied. However, he argues that Economic Capacity is not a valid measure of market power in cases involving utilities with retail load obligations, since most of the utility's Economic Capacity is committed to native load service during most periods and is thus not available to compete for sales to wholesale customers. Further, he argues that the screen failures in the Nevada Power market under these circumstances do not indicate that Nevada Power would have either the ability or incentive to raise prices or withhold capacity. He points out that Nevada Power is a net buyer with rapidly growing load of 3.3 percent per year for the next five years. He argues, therefore, that Nevada Power would have no economic incentive to withhold capacity in order to raise wholesale market prices.[12]

12. Further, Nevada Power does not have, and does not expect to have, market-based rates for power sales within its control area. According to Dr. Fox-Penner, the proposed transaction does not convey to Nevada Power the ability to raise prices unless Nevada Power's cost basis can be inflated through the proposed transaction, essentially flowing market power through into a cost-based rate, or present market prices in the region are significantly below Nevada Power's costs, and Nevada Power is not charging full cost-based rates. As noted by Applicants, Nevada Power is required to demonstrate to the Public Utility Commission of Nevada (Nevada Commission) that it is pursuing the lowest cost options for meeting its bundled retail loads, and Nevada Power has filed for the Nevada Commission's approval of the proposed transaction. Applicants note that Nevada Power's analysis of the proposed transaction before the Nevada Commission shows an estimated $262 million in present value savings for Nevada Power's customers as compared to alternative resource options. They conclude that the possibility that the proposed transaction will facilitate an increase in Nevada Power's cost-based rates seems remote.[13]

13. Dr. Fox-Penner states that the Available Economic Capacity measure is a better predictus of the possible competitive effects of the proposed transaction because it takes into account the utility's native load commitments. Using this measure, he finds only one screen failure in the Nevada Power market for the Spring-Peak season. However, he says that the market remains only moderately concentrated after the proposed transaction.

[11] Merger Policy Statement, Appendix A at 30,128.

[12] Fox-Penner Affidavit at P 63.

[13] Fox-Penner Affidavit at P 90, 91.

Breaking down this market period further, he states that it is characterized by a broad distribution of seller sizes. This market structure lends itself to competition far better than it does to either unilateral or multilateral strategic behavior.[14]

14. Dr. Fox-Penner argues, further, that the proposed transaction would free up transmission import capacity into the Nevada Power control area, allowing internal customers to purchase from trading hubs in the Western Electricity Coordinating Council.[15] His HHI analysis shows that the proposed transaction decreases the HHIs in the market under the Available Economic Capacity measure during three of the six super-peak periods.[16]

Commission Determination

15. We find Applicants' arguments persuasive. In *KCPL*, we discussed how we evaluate the results of the Delivered Price Test analysis when utilities dedicate some of their generation resources to native load.[17] Because of Nevada Power's significant native load obligation, with no foreseeable prospect of that obligation being lifted, we agree that Available Economic Capacity is the more relevant measure in the Nevada Power market and, therefore, should be given more weight. The only screen failure for Available Economic Capacity is in the Spring Peak season in the Nevada Power market, where the post-acquisition market is moderately concentrated and Nevada Power's market share is approximately 21 percent. We would be concerned with systematic screen failures in the

[14] Fox-Penner Affidavit at P 66.

[15] Fox-Penner Affidavit at P 67.

[16] The Herfindahl- Hirschman Index (HHI) is a widely accepted measure of market concentration. It is calculated by squaring the market share of each firm competing in the market and summing the results. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases. Markets in which the HHI is less than 1000 points are considered unconcentrated; markets in which the HHI is 1000 or more but less than 1800 are considered moderately concentrated; and markets where the HHI is 1800 or more are considered highly concentrated. The Commission has adopted the FTC/DOJ Horizontal Merger Guidelines, which state that, in a horizontal merger or acquisition, an increase of more than 50 HHI in a highly concentrated market or an increase of 100 HHI in a moderately concentrated market fails its screen and warrants further review.

[17] *Kansas City Power and Light Company,* 113 FERC ¶ 61,074 at P 35 (2005) (*KCPL*).

Nevada Power market if the market was highly concentrated and Nevada Power had a more significant market share. Here, there is no indication that the proposed transaction would create or enhance Nevada Power's ability to exercise market power.

b. Applicants' Analysis of Vertical Market Power Issues

16. Applicants argue that the proposed transaction will have no material effect on vertical market power as it relates to transmission. Nevada Power and Sierra Pacific Power Company both operate their transmission networks (which are not interconnected) under Commission-approved open access transmission tariffs (OATT). Applicants note that most of Nevada Power's wholesale buyers either own the transmission needed to serve their loads or have firm transmission rights to reach the regional wholesale market and therefore do not depend on Nevada Power for transmission access. Applicants state that under Nevada's restructuring legislation, any eligible retail customer that seeks to purchase from an alternative supplier is entitled to a *pro rata* share of Nevada Power's available import capability.[18]

17. Applicants argue that the proposed transaction has no effect on any of the aforementioned arrangements or requirements. Instead, it has a positive impact on transmission availability, because it slightly increases the amount of transfer capability available to wholesale customers within Nevada Power's control area and thereby reduces Nevada Power's reliance on power imports.[19] Applicants refer to Mr. Brian Whalen's testimony to support their assertion.[20] His testimony states that the proposed transaction will increase the available import capacity into Nevada Power by approximately 500 MWs in the highest peak hour in summer 2006.[21] Applicants state

[18] Application at 17, 18.

[19] Application at 18.

[20] Mr. Whalen, a Nevada Power employee, performed the analyses to determine the transmission network and transfer capabilities of Nevada Power and its surrounding areas. Mr. Whalen calculated the 2006 Availability Operating Transfer Capability for the transmission network used in Dr. Fox-Penner's Delivered Price Test analysis. In addition, Mr. Whalen sponsors all of the Operating Transfer Capabilities, Total Transfer Capabilities and "base flows" values for 2006 employed by Dr. Fox-Penner in his analysis.

[21] Whalen Affidavit at P 63.

that the proposed transaction would not increase Nevada Power's incentive to restrict customer access to supply alternatives via foreclosure,[22] nor would it change Nevada Power's ability to foreclose rival generators.[23]

Commission Determination

18. We find that the proposed transfer of Silverhawk Station to Nevada Power, which will add generation to Nevada Power's existing generation and transmission assets, will not harm competition or raise problems of vertical market power. In the Merger Policy Statement, we stated that, in order for a merger to create or enhance vertical market power, both the upstream and downstream markets must be highly concentrated.[24] Applicants have demonstrated that Economic Capacity is not the most relevant measure for determining competitive impacts in this case. Applicants also have demonstrated that, when the Available Economic Capacity measure is used, the relevant downstream market is not highly concentrated, nor will it be after the proposed transaction. Thus, there would not be the possibility of market foreclosure or raising rivals' costs in order to harm competition. Applicants also have explained that many of the wholesale customers own their own transmission assets and, therefore, could not be foreclosed by Nevada Power. We note that neither Nevada Power nor any of its affiliates control upstream fuel supplies that could be used to harm competition in downstream wholesale electricity markets.

2. Effect on Rates

a. Applicants' Analysis

19. Applicants state that the proposed transaction will have no adverse impact on rates charged for wholesale power or transmission. They state that all of Nevada Power's wholesale customers are served under long-term, fixed-price contracts that will not be affected by the proposed transaction. Nevada Power's transmission customers are served pursuant to Nevada Power's OATT, which will not be affected by the proposed transaction.

b. Commission Determination

20. Applicants have shown that the proposed transaction will not adversely affect the wholesale rates of any customers.

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[22] Fox-Penner Affidavit at P 99.

[23] Fox-Penner Affidavit at P 101.

[24] Order No. 642 at 31,911.

3. Effect on Regulation

a. Applicants' Analysis

21. Nevada Power's retail operations are subject to state regulation in Nevada, which will not be affected by the proposed transaction. They note that GenWest currently is subject to the Commission's jurisdiction, but following consummation of the proposed transaction, it will not have any jurisdictional assets, other than its tariff and contracts, which will be terminated pursuant to a separate filing.[25]

b. Commission Determination

22. As explained in the Merger Policy Statement and the Revised Filing Requirements, the Commission's primary concern with the effect on regulation of a proposed transaction involves possible changes in the Commission's jurisdiction that would diminish Commission authority to protect ratepayers against affiliate abuse. We also are concerned that a regulatory gap may arise at the state level should the affected state commission lack authority to act on the proposed merger.

23. We note that no entity has raised concerns about the proposed transaction's effect on state or federal regulation. No state has indicated that it lacks jurisdiction to consider the proposed transaction's effect on retail rates, and no state commission has intervened in this proceeding. Moreover, the proposed transaction will not create a registered holding company under the PUHCA 1935, thereby invoking the jurisdiction of the Securities and Exchange Commission. We, therefore, find that the proposed transaction will impair neither state nor federal regulation.

4. Accounting Treatment

24. Applicants submitted their proposed journal entries to account for the proposed transaction. The proposed accounting appears consistent with the Commission's Uniform System of Accounts. However, since this transfer of assets is a sale and acquisition of an operating unit or system, Applicants must file their proposed journal entries in Account 102, Electric Plant Purchased or Sold, as required by the instructions to such account, within six months of the date the transfer is consummated.[26]

The Commission orders:

(A) The proposed transaction is authorized upon the terms and conditions and for the purposes set forth in the application.

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[25] Application at 21-22.

[26] 18 C.F.R. Part 101 (2005).

(B) The foregoing authorization is without prejudice to the authority of the Commission or any other regulatory body with respect to rates, service, accounts, valuation, estimates or determinations of costs, or any other matter whatsoever new pending or which may come before this Commission.

(C) The Commission retains the authority under sections 203(b) and 309 of the FPA to issue supplemental orders as appropriate.

(D) Applicants shall make appropriate filings under section 205 of the FPA, as necessary, to implement the transaction.

(E) If the transaction results in changes in the status or the upstream ownership of Applicants' affiliated qualifying facilities, if any, a filing for recertification pursuant to 18 C.F.R. § 192.202 shall be made.

(F) Nevada Power and GenWest shall account for the transfer of the facilities in accordance with Electric Plant Instruction No. 5 and Account 102, Electric Plant Purchased or Sold, of the Uniform System of Accounts. Nevada Power also must file its proposed accounting within six months of the date that the transfer is consummated.

(G) Applicants shall notify the Commission within 10 days of the date of the disposition and acquisition of jurisdictional facilities has been consummated.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.